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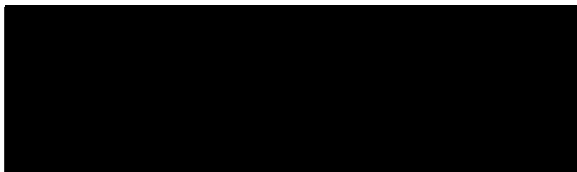
Secretary
Public Accounts and Estimates Committee
Legislative Assembly
Parliament of Victoria
Spring Street
Melbourne Vic 3000

9 November 2011

Dear Sir

Please find enclosed submission to your committee's inquiry into strengthening capacity for delivering significant infrastructure projects.

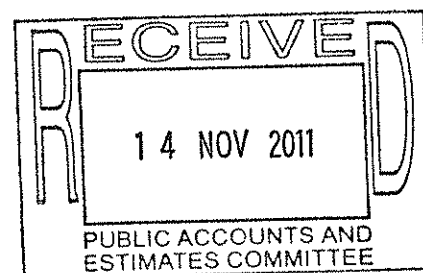
Yours sincerely

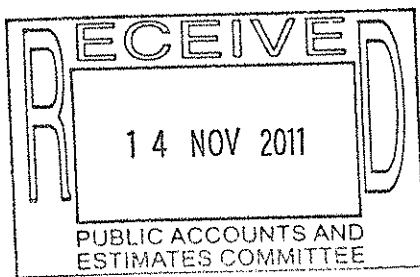


Lindsay Tanner
Special Advisor, Lazard Australia

Public Accounts and Estimates Committee

Submission No. 14





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PUBLIC SECTOR SKILLS AND INFRASTRUCTURE FINANCING

The process of financing major infrastructure projects has evolved into an extremely complex and challenging one. While the potential gains from innovative financing arrangements can be substantial, instruments like public-private partnerships (PPPs) impose a heavy capability burden upon the public sector. The mixed history of PPPs in Australia suggests that the public sector has not always been able to discharge that burden adequately.

The PPP model has several difficulties in the contemporary Australian context:

- Tender costs are widely regarded as excessive, even prohibitive
- Competition in the major construction sector is limited
- Intermediary fees are seen as excessive, undermining the incentive for long-term investors to invest
- Risk transfer issues are often problematic
- Where ongoing contract management is an issue, retaining contract management skills in the public sector when the primary activity is outsourced can be difficult
- Major projects typically involve a mixture of commercial and public policy issues: managing this intersection involves skills in short supply
- The absence of a predictable national pipeline of PPP projects makes it hard for investors to commit resources to this asset class
- Vague and uncertain contract clauses can lead to serious disputation
- Complex project management skills are in short supply around the world, and difficult to sustain in the public sector

The mix and level of skills available within government is obviously a critical part of this picture. Understanding what is required, and where it will be necessary to hire external specialists, is a key issue for government.

Among participants in the PPP area, the Victorian Government is generally recognized as having a better set of capabilities in this area than other jurisdictions in Australia. This does not mean there is no room for improvement, but it is important to acknowledge that Victoria faces these PPP challenges from a position

of relative strength. Over the past two decades, through privatizations and PPPs, Victoria has built up a considerable bank of experience and expertise.

The most important issues that should be noted in approaching these questions are:

- It is vital that some of the key players in Treasury have relevant high-level private sector experience
- Those who are given responsibility for handling a PPP process must be allowed maximum discretion to exercise personal judgment in order to maximize outcomes for the State
- In order to retain skills and people, the State needs a longer term plan for infrastructure financing that ensures there will be appropriate work for them to undertake in the future
- Innovative options for remunerating such people through success fee arrangements should be explored, provided that criteria are objective and performance is assessed well after the infrastructure is operational
- External specialist expertise is crucial: in several very specialized disciplines, it is neither feasible nor economic for the State to maintain in-house capability.

The relationship between key public sector staff and external advisors is absolutely critical to the success of a major project. Typically a project will need external legal, financial and commercial advisors. It is unrealistic to expect that the State will be able to employ the best legal advisors, the best accounting advisors, and the best commercial advisors in-house. With billions of dollars sometimes at stake, it is essential that the best advisors are involved. The client – in this case the State – needs to be in a position to extract maximum benefit from their advice. That means being able to fully understand and analyse it, and provide appropriate advice to the government which takes this specialized external advice properly into account.

Anyone who has high-level corporate sector experience of managing a major project or takeover involving complex legal, financial and commercial decisions would be well credentialed to work in Treasury managing a major PPP project. Because PPP projects usually involve complex public policy issues, other skills and experience are also necessary, but they can be assumed to already be present.